

STATE OF NEW YORK INSURANCE DEPARTMENT

REPORT ON EXAMINATION

OF THE

FIRST SECURITY BENEFIT LIFE INSURANCE

AND ANNUITY COMPANY OF NEW YORK

AS OF

DECEMBER 31, 2000

DATE OF REPORT:

JANUARY 11, 2002

EXAMINER:

PHARES U. CATON

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STATE OF NEW YORK
INSURANCE DEPARTMENT
25 BEAVER STREET
NEW YORK, NEW YORK 10004

January 11, 2002

Honorable Gregory V. Serio
Superintendent of Insurance
Albany, New York 12257

Sir:

In accordance with instructions contained in Appointment No. 21774, dated September 10, 2001 and annexed hereto, an examination has been made into the condition and affairs of First Security Benefit Life Insurance and Annuity Company of New York, hereinafter referred to as "the Company," at its home office located at 70 West Red Oak Lane, White Plains, New York 10604.

Wherever "Department" appears in this report, it refers to the State of New York Insurance Department.

The report indicating the results of this examination is respectfully submitted.

1. EXECUTIVE SUMMARY

The examiner's review of a sample of transactions did not reveal any differences which materially affected the Company's financial condition as presented in its financial statements contained in the December 31, 2000 filed annual statement. (See item 5 of this report)

The examiner's review of the Company's market conduct activities did not reveal significant instances which deviated from the New York Insurance Law, Department regulations and circular letters and the operating rules of the Company. (See item 6 of this report)

2. SCOPE OF EXAMINATION

The prior examination was conducted as of December 31, 1997. This examination covers the period from January 1, 1998 through December 31, 2000. As necessary, the examiner reviewed transactions occurring subsequent to December 31, 2000 but prior to the date of this report (i.e., the completion date of the examination).

The examination comprised a verification of assets and liabilities as of December 31, 2000 to determine whether the Company's 2000 filed annual statement fairly presents its financial condition. The examiner reviewed the Company's income and disbursements necessary to accomplish such verification and utilized the National Association of Insurance Commissioners' Examiners Handbook or such other examination procedures, as deemed appropriate, in such review and in the review or audit of the following matters:

- Company history
- Management and control
- Corporate records
- Territory and plan of operation
- Market conduct activities
- Growth of Company
- Business in force by states
- Mortality and loss experience
- Reinsurance
- Accounts and records
- Financial statements

The examiner reviewed the corrective actions taken by the Company with respect to violations and recommendations contained in the prior report on examination. The results of the examiner's review are contained in item 7 of this report.

This report on examination is confined to financial statements and comments on those matters which involve departure from laws, regulations or rules, or which require explanation or description.

3. DESCRIPTION OF COMPANY

A. History

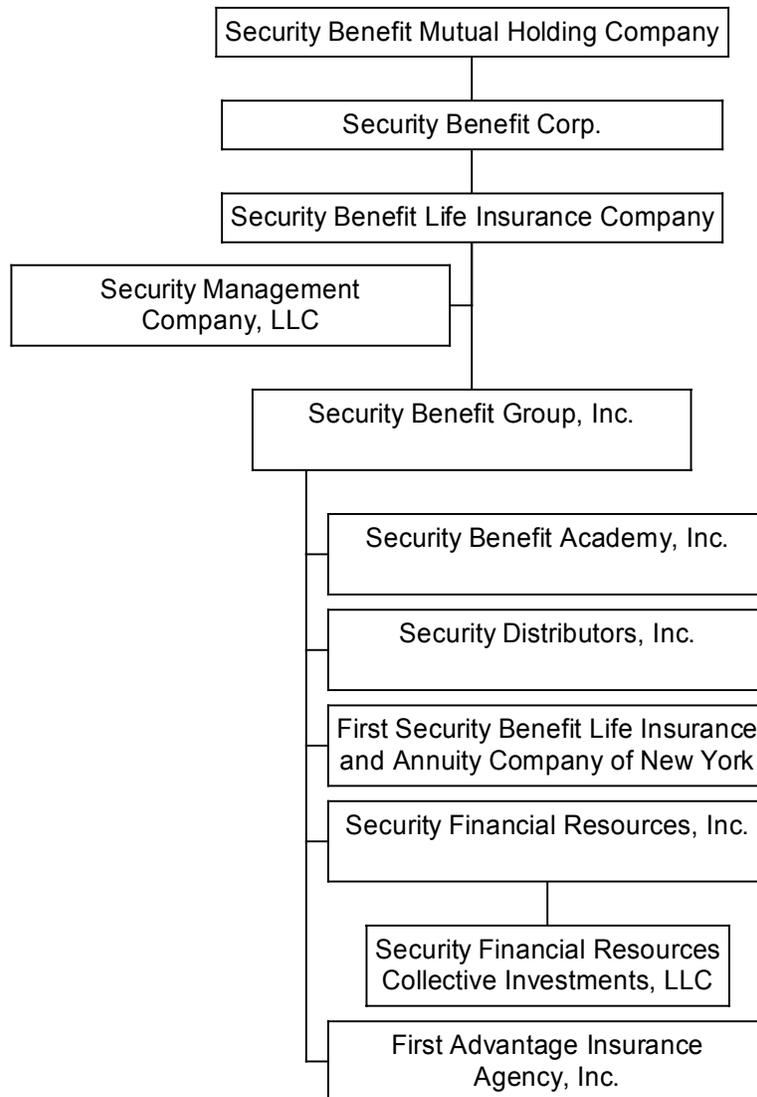
The Company was incorporated as a stock life insurance company under the laws of New York on November 8, 1994, was licensed on July 31, 1995 and commenced business on that same date. Initial resources of \$6,000,000, consisting of common capital stock of \$2,000,000 and paid in and contributed surplus of \$4,000,000, were provided through the sale of 200,000 shares of common stock (with a par value of \$10 each) for \$30 per share to Security Benefit Life Insurance Company (“SBL”), a Kansas life insurance company. Subsequently, on February 24, 1995, all of the stock was transferred to Security Benefit Group, Inc. (“SBG”), a wholly owned subsidiary of SBL.

On September 8, 1995, the Company merged with Pioneer National Life Insurance Company (“PNL”), a stock life insurance company organized under the laws of the state of Kansas. As of that date, PNL ceased to exist and First Security Benefit Life Insurance and Annuity Company of New York became the surviving company. As a result of this transaction, the Company’s paid in and contributed surplus was increased to \$4,600,000.

B. Holding Company

The Company is a wholly owned subsidiary of SBG, a Kansas corporation, which is a holding company and a management services company. SBG is a wholly owned subsidiary of SBL, a Kansas life insurance company, which in turn is a wholly owned subsidiary of Security Benefit Corp., (“SBC”), a Kansas holding company. The ultimate parent of the Company is Security Benefit Mutual Holding Company (“SBMHC”), a Kansas corporation.

An organization chart reflecting the relationship between the Company and significant entities in its holding company system as of December 31, 2000 follows:



The Company had three service agreements in effect as of December 31, 2000. The first agreement is with SBL, whereby SBL provides the Company with underwriting, claims, actuarial and disaster recovery services. The second agreement is with SBG, whereby SBG provides accounting, marketing, advertising support and disaster recovery services. The third agreement is with SBL, whereby SBL provides investment services for the Company.

The Company also has a tax allocation agreement with SBL, whereby the Company elected to file its federal income tax returns on a consolidated basis.

The service agreements with SBL and SBG indicate that those companies are to provide disaster recovery services to the Company. The examiner was informed that a working disaster recovery plan is in place; however, the disaster recovery plan has not been tested since April 1997. The examiner was also informed that the companies are currently updating the disaster recovery plan to include a business continuity plan.

The examiner recommends that the Company's disaster recovery plan include provisions for periodical testing and that such testing be put into practice. The test plans and results (indicating problems found or successful completions) and indication of management approval should be maintained. In addition, the disaster recovery plan should be aligned with the Company's business continuity plan, which is currently under development. The examiner also recommends that the Company continue with the development of its business continuity plan until it is completed. Both the disaster recovery plan and the business continuity plan should be approved and periodically reviewed by Company management to ensure that they meet the needs of the business.

The service agreements with both companies also state that an annual cost analysis should be done to determine, as closely as possible, the actual costs of services rendered and facilities used. SBG and SBL are utilizing a study done in 1998 to allocate costs to the Company.

The examiner recommends that an annual cost analysis be performed as required by the service agreements.

C. Management

The Company's by-laws provide that the board of directors shall be comprised of not less than nine and not more than 21 directors. Directors are elected for a period of one year at the annual meeting of the stockholders held in April of each year. As of December 31, 2000, the board of directors consisted of nine members. Meetings of the board are held quarterly.

The nine board members and their principal business affiliation, as of December 31, 2000, were as follows:

| <u>Name and Residence</u> | <u>Principal Business Affiliation</u> | <u>Year First Elected</u> |
|---|---|---------------------------|
| Stephen A. Crane* New York, NY | Chairman, President and Chief Executive Officer Sterling & Cooke | 1999 |
| Howard R. Fricke Topeka, KS | Chairman of the Board and Chief Executive Officer First Security Benefit Life Insurance and Annuity Company of New York | 1994 |
| John E. Hayes, Jr.* Belleair Shore, FL | Retired, Chairman and Chief Executive Officer Western Resources, Inc. | 1994 |
| Stephen R. Herbert* Pound Ridge, NY | Attorney Locke & Herbert | 1998 |
| Kris A. Robbins Topeka, KS | President First Security Benefit Life Insurance and Annuity Company of New York | 1998 |
| Donald J. Schepker Topeka, KS | Vice President First Security Benefit Life Insurance and Annuity Company of New York | 1994 |
| James R. Schmank Topeka, KS | Vice President and Treasurer First Security Benefit Life Insurance and Annuity Company of New York | 1996 |
| Roger K. Viola Topeka, KS | Vice President, General Counsel and Secretary First Security Benefit Life Insurance and Annuity Company of New York | 1994 |
| Katherine P. White* New York, NY | Attorney AT&T | 1994 |

* Not affiliated with the Company or any other company in the holding company system

The examiner's review of the minutes of the meetings of the board of directors and its committees indicated that meetings were well attended and that each director attended a majority of meetings.

The following is a listing of the principal officers of the Company as of December 31, 2000:

| <u>Name</u> | <u>Title</u> |
|--------------------|--|
| Howard R. Fricke | Chief Executive Officer |
| Kris A. Robbins | President |
| Donald J. Schepker | Vice President |
| James R. Schmank | Vice President, Treasurer |
| Roger K. Viola | Vice President, General Counsel and Secretary |
| John T. Gaule | Actuary |
| Peggy Avey* | Chief Administrative Officer and Assistant Secretary |

* Designated consumer services officer per Section 216.4(c) of Department Regulation No. 64

D. Territory and Plan of Operation

The Company is authorized to write life insurance, annuities and accident and health insurance as defined in paragraphs 1, 2 and 3 of Section 1113(a) of the New York Insurance Law.

The Company is licensed to transact business in two states, namely New York and Kansas. In 2000, all annuity considerations were received from New York. In addition, 80% of life insurance premiums were received from Kansas as a result of the merger with PNL.

The Company sells only variable annuities and does not engage in the sale of life or accident and health insurance. The Company, however, inherited some life insurance policies from PNL that are reinsured with SBL and are currently in runoff.

The Company's only product is a flexible premium variable annuity marketed through direct response mailings. T. Rowe Price Associates, Inc., an investment adviser, registered with the Securities and Exchange Commission ("SEC"), manages the underlining investments of the contracts. T. Rowe Price Investment Services, Inc., a wholly owned subsidiary of T. Rowe Price Associates, Inc. and a broker/dealer registered with the SEC, is the appointed distributor of the contracts.

E. Reinsurance

As of December 31, 2000, the Company had a reinsurance treaty in effect with SBL, an accredited reinsurer, to reinsure, on a 100% coinsurance basis, the life insurance policies that

were inherited from PNL when the Company and PNL merged. The total face amount of life insurance ceded as of December 31, 2000 was \$316,852. As of December 31, 2000 this closed block of business was comprised of 131 policies in force.

4. SIGNIFICANT OPERATING RESULTS

Indicated below is significant information concerning the operations of the Company during the period under examination as extracted from its filed annual statements. Failure of items to add to the totals shown in any table in this report is due to rounding.

The following table indicates the Company's financial growth during the period under review:

| | <u>December 31,</u> <u>1997</u> | <u>December 31,</u> <u>2000</u> | <u>Increase</u> |
|--|------------------------------------|------------------------------------|--------------------|
| Admitted assets | <u>\$21,720,138</u> | <u>\$25,001,775</u> | <u>\$3,281,637</u> |
| Liabilities | <u>\$15,031,188</u> | <u>\$18,079,035</u> | <u>\$3,047,847</u> |
| Common capital stock | \$ 2,000,000 | \$ 2,000,000 | \$ 0 |
| Gross paid in and contributed surplus | 4,600,000 | 4,600,000 | 0 |
| Unassigned funds (surplus) | <u>88,950</u> | <u>322,740</u> | <u>233,790</u> |
| Total capital and surplus | <u>\$ 6,688,950</u> | <u>\$ 6,922,740</u> | <u>\$ 233,790</u> |
| Total liabilities, capital and surplus | <u>\$21,720,138</u> | <u>\$25,001,775</u> | <u>\$3,281,637</u> |

The majority (68%) of the Company's admitted assets, as of December 31, 2000, was derived from Separate Accounts.

The Company's invested assets, as of December 31, 2000, exclusive of separate accounts, were mainly comprised of bonds (96%).

The Company's entire bond portfolio, as of December 31, 2000, was comprised of investment grade obligations.

The net gain after federal income taxes but before realized capital gains (losses) was solely attributable to individual annuities for the entire examination period; the amounts reported were \$28,771 in 1998, \$21,636 in 1999 and \$56,755 in 2000.

5. FINANCIAL STATEMENTS

The following statements show the assets, liabilities, capital, surplus and other funds as of December 31, 2000, as contained in the Company's 2000 filed annual statement, a condensed summary of operations and a reconciliation of the capital and surplus account for each of the years under review. The examiner's review of a sample of transactions did not reveal any differences which materially affected the Company's financial condition as presented in its financial statements contained in the December 31, 2000 filed annual statement.

A. ASSETS, LIABILITIES, CAPITAL, SURPLUS AND OTHER FUNDS AS OF DECEMBER 31, 2000

Admitted Assets

| | |
|--|---------------------|
| Bonds | \$ 6,903,988 |
| Cash and short term investments | 266,015 |
| Investment income due and accrued | 119,437 |
| Actuarial risk fees & mortality adjustments due from Separate Accounts | 535 |
| Miscellaneous assets | 3,284 |
| From Separate Accounts statement | <u>17,708,516</u> |
| Total admitted assets | <u>\$25,001,775</u> |

Liabilities, Capital, Surplus and Other Funds

| | |
|---|-------------------------|
| Aggregate reserve for life policies and contracts | \$ 321,285 |
| General expenses due or accrued | 11,706 |
| Taxes, licenses and fees due or accrued | 35,462 |
| Federal income taxes due or accrued | (6,810) |
| Amounts withheld or retained by company as agent or trustee | 1,191 |
| Miscellaneous liabilities: | |
| Asset valuation reserve | 6,809 |
| Payable to parent, subsidiaries and affiliates | 491 |
| Miscellaneous liabilities | 385 |
| From Separate Accounts statement | <u>17,708,516</u> |
| Total liabilities | <u>\$18,079,035</u> |
| Common capital stock | \$ 2,000,000 |
| Gross paid in and contributed surplus | 4,600,000 |
| Unassigned funds (surplus) | <u>322,740</u> |
| Total capital, surplus and other funds | <u>\$ 6,922,740</u> |
| Total liabilities, capital, surplus and other funds | <u>\$25,001,775</u> |

B. CONDENSED SUMMARY OF OPERATIONS

| | <u>1998</u> | <u>1999</u> | <u>2000</u> |
|---|--------------------|--------------------|---------------------|
| Premiums and considerations | \$3,591,232 | \$1,349,024 | \$ 1,119,394 |
| Investment income | 441,843 | 407,323 | 421,758 |
| Miscellaneous income | <u>92,439</u> | <u>103,635</u> | <u>99,466</u> |
| Total income | <u>\$4,125,514</u> | <u>\$1,859,982</u> | <u>\$ 1,640,618</u> |
| Benefit payments | \$1,464,630 | \$2,061,716 | \$ 3,473,207 |
| Increase in reserves | (20,569) | (4,297) | (20,431) |
| General expenses and taxes | 436,164 | 470,153 | 433,171 |
| Net transfers to (from) Separate Accounts | <u>2,165,674</u> | <u>(692,077)</u> | <u>(2,325,881)</u> |
| Total deductions | <u>\$4,045,899</u> | <u>\$1,835,495</u> | <u>\$ 1,560,066</u> |
| Net gain | \$ 79,615 | \$ 24,487 | \$ 80,552 |
| Federal income taxes | <u>50,844</u> | <u>2,851</u> | <u>23,797</u> |
| Net income | <u>\$ 28,771</u> | <u>\$ 21,636</u> | <u>\$ 56,755</u> |

C. CAPITAL AND SURPLUS ACCOUNT

| | <u>1998</u> | <u>1999</u> | <u>2000</u> |
|--|--------------------|--------------------|--------------------|
| Capital and surplus, December 31, prior year | <u>\$6,688,950</u> | <u>\$6,759,691</u> | <u>\$6,826,351</u> |
| Net income | \$ 28,771 | \$ 21,636 | \$ 56,755 |
| Change in non admitted assets And related items | 40,956 | 40,968 | 40,209 |
| Change in asset valuation reserve | 921 | (664) | (575) |
| Prior year correction | <u>93</u> | <u>4,720</u> | <u>0</u> |
| Net change in capital and surplus | <u>\$ 70,741</u> | <u>\$ 66,660</u> | <u>\$ 96,389</u> |
| Capital and surplus, December 31, current year | <u>\$6,759,691</u> | <u>\$6,826,351</u> | <u>\$6,922,740</u> |

6. MARKET CONDUCT ACTIVITIES

The examiner reviewed various elements of the Company's market conduct activities affecting policyholders, claimants, and beneficiaries to determine compliance with applicable statutes and regulations and the operating rules of the Company.

A. Advertising and Sales Activities

The examiner reviewed a sample of the Company's advertising files and the sales activities of the agency force including trade practices, solicitation and the replacement of insurance policies.

Based upon the sample reviewed, no significant findings were noted.

B. Underwriting and Policy Forms

The examiner reviewed a sample of new underwriting files, both issued and declined, and the applicable policy forms.

Based upon the sample reviewed, no significant findings were noted.

C. Treatment of Policyholders

The examiner reviewed a sample of various types of claims, surrenders, changes and lapses. The examiner also reviewed the various controls involved, checked the accuracy of the computations and traced the accounting data to the books of account.

Based upon the sample reviewed, no significant findings were noted.

D. Response to Supplement No. 1 to Department Circular Letter No. 19 (2000)

Supplement No. 1 to Circular Letter No. 19 (2000) (the "Supplement"), issued by the Department on June 22, 2000, notified all licensed life insurers that the Department was investigating allegations of race-based underwriting of life insurance by its licensees. The Supplement directed, pursuant to Section 308 of the New York Insurance Law, each domestic and foreign life insurer to review its past and present underwriting practices regarding race-based underwriting and to report its findings to the Department, no later than August 15, 2000.

Pursuant to Section 308 of the New York Insurance Law, the Company submitted in a timely manner a report of the findings of its review of past and present underwriting practices regarding race-based underwriting made in accordance with the requirements of the Supplement.

The Company's review consisted of a review of the underwriting and rating practices of the life insurance business obtained by reinsurance assumption from PNL.

A review was made into the affairs of the Company with respect to race based underwriting and the findings reported pursuant to the Supplement. The examiner determined that the Company's review of its past and present underwriting practices complied with the requirements of the Supplement. Based upon the procedures performed, the examiner noted no discrepancies from the Company's reported findings and no instances of race-based underwriting.

7. PRIOR REPORT SUMMARY AND CONCLUSIONS

Following are the violations and recommendations contained in the prior report on examination and the subsequent actions taken by the Company in response to each citation:

| <u>Item</u> | <u>Description</u> |
|-------------|---|
| A | <p>The examiner recommends that the Company sign the agreement with Bank One that allows the bank to transfer money between the annuitant's accounts.</p> <p>The agreement was signed.</p> |
| B | <p>The examiner recommends that the Company utilize Department Regulation No. 33 when formulating a method of expense allocation.</p> <p>The Company adopted a method of allocating income utilizing Department Regulation No. 33.</p> |
| C | <p>The examiner recommends that the Company take steps to ensure that electronic transactions are recorded in the cash journal in a timely manner.</p> <p>A review indicated that all transactions are now recorded in a timely manner.</p> |
| D | <p>The Company violated Section 2122(a)(2) of the New York Insurance Law by distributing sales material that referenced its unauthorized parent, SBL.</p> <p>The Company no longer references SBL in its sales material.</p> |
| E | <p>The Company violated Section 1313(f) of the New York Insurance Law by distributing sales material which referred to the assets of the holding company without mentioning the Company's assets.</p> <p>The Company no longer distributes these sales materials.</p> |
| F | <p>The Company violated Section 219.5(a) of Department Regulation No. 34-A by not maintaining its advertising files with a notation indicating the extent of distribution as required by such section.</p> <p>The Company now documents the extent of distribution.</p> |

| <u>Item</u> | <u>Description</u> |
|-------------|---|
| G | <p>The Company violated Section 219.4(p) of Department Regulation No. 34-A by not placing the Company's name prominently in the advertisements and by giving the impression that T. Rowe Price and not the insurer would be responsible for the financial obligations under the contracts.</p> <p>A review indicated that advertisements are now reviewed by the Company's General Counsel to ensure that the Company is identified clearly at all times.</p> |
| H | <p>The Company violated Section 3201(b)(1) of the New York Insurance Law by issuing annuities using an unapproved application form.</p> <p>The Company no longer uses the unapproved application form.</p> |
| I | <p>The examiner recommends that the Company maintain its claim files in a manner that complies with the requirements of Section 216.11 of Department Regulation No. 64.</p> <p>The Company now maintains claim files as required by Section 216.11 of Department Regulation No. 64.</p> |

8. SUMMARY AND CONCLUSIONS

Following are the recommendations contained in this report:

| <u>Item</u> | <u>Description</u> | <u>Page No(s).</u> |
|-------------|--|--------------------|
| A | The examiner recommends that the Company's disaster recovery plan include provisions for periodical testing and that such testing be put into practice. The test plans and results (indicating problems found or successful completions) and indication of management approval should be maintained. In addition, the disaster recovery plan should be aligned with the Company's business continuity plan, which is currently under development. The examiner also recommends that the Company continue with the development of its business continuity plan until it is completed. Both the disaster recovery plan and the business continuity plan should be approved and periodically reviewed by Company management to ensure that they meet the needs of the business. | 6 |
| B | The examiner recommends that an annual cost analysis be performed as required by the service agreements. | 6 |

APPOINTMENT NO. 21774

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, GREGORY V. SERIO, Superintendent of Insurance of the State of New York, pursuant to the provisions of the Insurance Law, do hereby appoint:

PHARES CATON

as a proper person to examine into the affairs of the

**FIRST SECURITY BENEFIT LIFE AND ANNUITY COMPANY
OF NEW YORK**

and to make a report to me in writing of the condition of the said

COMPANY

with such other information as he shall deem requisite.

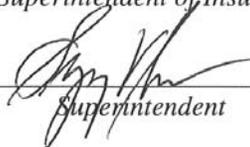
In Witness Whereof, I have hereunto subscribed by name
and affixed the official Seal of the Department
at the City of New York

this 10th day of September, 2001



GREGORY V. SERIO

Superintendent of Insurance


Superintendent